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EUROPEAN COMMISSION FINDS NEW TARGET: FRENCH MULTINATIONAL ENGIE (FORMERLY G.D.F. SUEZ)

The latest development in the E.U.'s ongoing fight against perceived illegal State Aid is the opening of an in-depth investigation into Luxembourg's tax treatment of the G.D.F. Suez group (now Engie). On January 5, 2017, the European Commission issued preliminary findings alleging illegal State Aid by the Luxembourg taxing authorities.

Two units of Engie, which received tax rulings from Luxembourg, helped the company to reduce its taxable base by up to €1.15 billion between 2009 and 2015 by causing group members to borrow money from one another using "ZORAs," certain interest-free convertible instruments. The European Commission considers the two transactions to be treated as both equity and debt, giving rise to "double non-taxation." The borrowers can significantly reduce their taxable profits in Luxembourg by deducting the provisioned interest payments, while, at the same time, the lenders are not taxed on the profits generated by the transaction because Luxembourg tax rules exempt income from equity investments. According to the European Commission, this confers a selective advantage on the Engie group companies, allowing them to reduce their taxable income in a manner not available to other companies using instruments similar to ZORAs.

For its part, Luxembourg has rejected these allegations and argued that the tax treatment granted under the tax rulings conforms with the country's domestic tax rules. In the event the European Commission's allegations are sustained, further litigation before the European Court of Justice ("E.C.J.") may ensue. If the tax arrangements are found to breach the E.U. rules on illegal State Aid, this case will have a tremendous impact, as Engie is the first European-based company to be investigated after Apple, Starbucks, and Fiat, and a third of the share capital of Engie is held by the French Republic.

FOREIGN TRUST DISCLOSURE PENALTIES UNDER REVIEW IN FRANCE

Under French tax law, trust disclosure obligations are imposed (i) if the trustee, the settlor, or at least one of the beneficiaries has a tax residence in France or (ii) when any of the assets or rights placed in the trust are located in France. Trustees are required to disclose the creation of the trust instrument, the names of the settlors and the beneficiaries, as well as the terms of the trust and any amendments made to

it.[1] Violation of this rule triggers penalties equal to the greater of €20,000 or 12.5% of the assets, rights, and capitalized incomes.[2]

Objections have been raised against the difference in the applicable penalties for French tax residents holding bank accounts abroad and individuals holding an interest in a trust. Failure to declare unreported foreign bank accounts is lower and subject to a €1,500 penalty (or €10,000 if the bank account is held in a country with which France has not signed a tax treaty containing an administrative assistance clause allowing access to bank information). The French Constitutional Court has been requested by the Administrative Court (*Conseil d'Etat*) to answer whether the provisions of Article 1736, IV *bis* of the French Tax Code violate the French Constitution and specifically the principle of proportionality between penalties and criminal offences.

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It should be noted that last October the French Constitutional Court ruled that the French Public Register of Trusts breached privacy rights and was unconstitutional. The register provided the date of creation of the trust, the identity of the trustee, the settlor(s), and the beneficiaries. The court declared that although the register was aimed at avoiding tax evasion, public access to the register constituted a disproportionate violation of the right to privacy.[3]

SPANISH TAX SCHEME INCOMPATIBLE WITH THE INTERNAL MARKET

In its decision in *Commission v. World Duty Free Group*, the E.C.J. agreed with the European Commission on the criteria upon which a measure by a Member State may be viewed as selective and therefore constitute illegal State Aid.

The Spanish provisions in question introduced a more favorable tax treatment for financial goodwill derived from a foreign acquisition. Under these new rules, in the event a company taxable in Spain acquires an interest in the share capital of a foreign company equal to at least 5% and holds that participation for an uninterrupted period of at least one year, the resulting goodwill may be deducted (in the form of an amortization) from the corporate income tax for which the undertaking is liable. To be classified as a "foreign company," a company must be subject to a similar tax in its country of origin and its income must derive mainly from business activities carried out abroad.

In a prior decision (which had been appealed to the E.C.J), the European General Court ("E.G.C.") annulled the European Commission's decision that Spain's regime allowing companies to amortize goodwill for acquisitions of foreign subsidiaries constituted State Aid.[4] The advocate general explained that a contrary decision could "lead to every tax measure the benefit of which is subject to certain conditions being found to be selective, even though . . . [other undertakings] would be capable of satisfying the conditions."

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1 Article 1649 AB of the French Tax Code.

2 Article 1736, IV *bis* of the French Tax Code.

3 Article 2 of the Declaration of Human Rights.

4 *Autogrill Espana, SA v. Commission*, Case T-219/10.

The E.C.J. found that the measure was selective because the tax benefit granted constitutes a derogation from the normal tax regime and discriminates between taxpayers in a comparable factual and legal situation. Generally, selectivity is shown if one commercial undertaking is favored over another. This ruling expands dramatically the application of the selectivity requirement.

TAX COURT UPHOLDS I.R.S. LIEN NOTICE AND NOTICE OF PROPOSED LEVY IN ESTATE OF MYERS

On January 10, the U.S. Tax Court held that the I.R.S. did not abuse its discretion when it failed to pursue collection from non-probate assets and certain jointly owned probate property, but rather filed a lien notice and notice of proposed levy against the estate.[5]

Ruben A. Myers died on November 15, 2005, leaving family farmland, other real property, and some liquid assets. Non-probate assets were also included in the taxable estate. On February 15, 2007, the executor filed a Federal estate tax return and started making installment payments until beginning of 2014. When the petitioner became delinquent to those payments, the I.R.S. issued a Notice of Federal Tax Lien ("N.F.T.L.") and then a Notice of Intent to Levy ("N.I.L.").

After the petitioner appealed, the I.R.S. stopped all collection activity, and did not begin collection actions against the transferees of the non-probate assets. The special estate tax lien provided for in Code §6324 expired on November 15, 2015. The petitioner alleged that "the Commissioner abused his discretion by failing to file a lien against the non-probate assets" and proceeding to collect from probate assets (family farmland).

The Tax Court held that:

> The statute does not give us license to conduct a broad-ranging inquiry into the means by which respondent [the I.R.S.] has sought to collect estate tax from petitioner over the many years since decedent's death. Our focus is a narrow one: We ask only whether SO Harding [the I.R.S. agent] abused his discretion in sustaining the filing of the lien notice and the proposed levy action.

The Tax Court held that the I.R.S. did not abuse its discretion by failing to collect from non-probate assets before collecting from the estate. In a nod to the estate, the Tax Court noted, however, that it might still be possible for the I.R.S. to seek collection from third-party recipients under the rules applicable to transferees. What is important to note is while the I.R.S.'s ability to collect tax that is properly owing is broad, its actions are not necessarily designed to be taxpayer-friendly.

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[5] *Estate of Myers v. Commr.*, T.C. Memo 2017-11.

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